

cost recovery process under regulation. This process allows utilities to recover their recurring expenses and depreciable fixed costs through rates charged to customers. The “bottom-up” category includes methodologies that are also used in regulatory proceedings, but they are more detailed and complex and have more extensive data receipts. This category includes models that combine production cost simulations –with financial analyses. Research Triangle Institute (RTI) applied both types of methodologies in this study. An overview of the two Excel spreadsheet models we used is presented in Volume 3.

Because several key assumptions and policy choices affect stranded costs, we discuss each of them in this volume. They are as follows:

1. start date of retail competition;
2. whether nexus is established for tax purposes;
3. the price of retail power in a competitive environment;
4. the discount rate used to convert a utility’s stream of annual stranded costs into a lump sum value (net present value) at the start date of retail competition;
5. the length of the analysis period, which we believe should extend through the design life of existing generating assets, but which policymakers may choose to restrict to shorter time horizons. For example, policymakers may choose to end the analysis period once annual “negative” stranded costs begin to appear (i.e., whenever the projected regulated price of power falls below the projected competitive price power); and
6. whether “cap adds” are included in stranded costs.